Supreme Court, U. S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1979

No. 79-2054

HARRY LEWIS, ALFRED B. REISS, CAROLA GRUEN, as Executrix of the estate of her late husband, Theodore Gruen, IRA BARMARK and COLONIAL SECURITIES CORPORATION,

Petitioners,

—v—

HAROLD W. McGRAW, JR., JOHN L. McGRAW, DANIEL F. CROWLEY, PETER O. LAWSON-JOHNSTON, KAY K. MAZUY, WILLIAM J. McGILL, GORDON W. McKINLEY, ALAN J. PIFER, LOUIS PUTZE, HOWARD S. TUTHILL, JAMES E. WEBB, VERNON R. ALDEN, GEORGE R. WEBSTER and McGRAW-HILL, INC.,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Petitioners pray that a writ of certiorari issue to review the judgment entered on April 3, 1980, by the United States Court of Appeals for the Second Circuit, which judgment affirmed a judgment of the United States District Court for the Southern District of New York dismissing petitioners' complaint, brought under the Williams Act, Section 14(e) of the Securities Exchange Act of 1934, 15 U.S.C. §78n(e), on the grounds that there was (i) a lack of jurisdiction over the subject matter and (ii) a failure to state a claim for which relief can be granted.

Opinions Below

The opinion of the United States Court of Appeals for the Second Circuit, filed April 3, 1980, has not yet been officially reported and is set forth in Appendix A hereto.* The opinion of the United States District Court for the Southern District of New York, filed November 30, 1979, has not yet been officially reported and is set forth in Appendix B hereto.**

Jurisdiction

The judgment of the Court of Appeals was entered on April 3, 1980. No petition for rehearing was filed. This Court's jurisdiction is invoked under 28 U.S.C. Section 1254(1).

Question Presented

Is the Williams Act violated when persons opposing a tender offer make untrue statements of material facts and omit to state other material facts, and otherwise engage in fraudulent, deceptive and manipulative practices in connection with the tender offer, where the very misconduct alleged deprives the shareholders of the opportunity to accept the tender offer?

Statute Involved

The Williams Act, Section 14(e) of the Securities Exchange Act of 1934 (15 U.S.C. §78n(e)), provides as follows:

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* The opinion is reprinted at [Current Binder] CCH Fed. Sec. L. Rep. ¶97,344 (2d Cir. 1980).

** The opinion is reprinted at [Current Binder] CCH Fed. Sec. L. Rep. ¶97,195 (S.D.N.Y. 1979).

"It shall be unlawful for any person to make any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, or to engage in any fraudulent, deceptive, or manipulative acts or practices, in connection with any tender offer or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any such offer, request, or invitation."

Statement of the Case

A. *The Complaint*

Plaintiffs served a consolidated amended complaint (the "complaint") alleging that the individual defendants, who were directors of defendant McGraw-Hill, Inc. ("McGraw-Hill"), violated the Williams Act when they attacked, with material untruths and omissions, a tender offer by American Express Company ("American Express"). Plaintiffs have brought the case as a class action on behalf of all persons who were McGraw-Hill shareholders on January 31, 1979, the date that McGraw-Hill made its rejection of the American Express offer final.

The essence of the complaint is that defendants violated the Williams Act when they bitterly fought the announced American Express offer with a barrage of material falsehoods and omissions. As set forth in the complaint, although defendants vilified American Express in public (by indicating, among other things, that American Express had illegally complied with the Arab boycott, and that the offer violated the federal Bank Holding Act), defendants omitted to state the most material fact of all: that is, just a few months prior the same McGraw-Hill had

advised the very same American Express that it (McGraw-Hill) was favorably considering a merger with American Express.

Furthermore, although the McGraw-Hill stock was trading on the New York Stock Exchange at approximately $25 per share, McGraw-Hill announced (falsely) that the $40 per share offer by American Express was inadequate. Defendants went on to mischaracterize the American Express offer as "reckless", "illegal", and "improper", descriptions that were as knowingly false as defendants' description of the $40 price as "inadequate". By use of their "scorched earth" policy (as so described by the press), defendants illegally thwarted the American Express tender offer. Upon abandonment of the offer, McGraw-Hill's stock returned to its pre-offer price of $25 per share.

As set forth in the complaint, had defendants told the truth and the whole truth about the American Express proposal, the tender offer would, necessarily, have gone forward at a price of at least $40 per share. Had the truth been told (i.e., defendants knew that American Express was a distinguished company and that $40 per share was a fair price), plaintiffs could have sought injunctive relief and, more importantly, the reasons for accepting the high offer would have been compelling and irresistible. Therefore, the McGraw-Hill shareholders were damaged when defendants were able to defeat American Express's offer to buy all the outstanding shares of McGraw-Hill at $40 per share (representing a 50% premium over the pre-tender offer market price).

B. *Defendants' Motion*

Defendants moved pursuant to Rules 12(b)(1) and (6) of the Federal Rules of Civil Procedure for an order dis-

missing the complaint for lack of federal jurisdiction over the subject matter and for failure to state a claim for which relief can be granted.

In particular, defendants argued that their conduct had not been "in connection with" a tender offer, hence the Williams Act was inoperative; that under this Court's decision in *Santa Fe Industries* v. *Green,* 430 U.S. 462 (1977), plaintiffs were relegated to the state courts since the action alleged only a breach of fiduciary duty; and that plaintiffs could not have relied on any alleged misconduct because the tender offer was thwarted before the shareholders had an opportunity to accept it.

C. *The District Court's Decision*

The District Court (per Motley, J.) agreed with plaintiffs that the alleged misstatement and omissions were "in connection with" the American Express offer, and that *Santa Fe Industries* v. *Green, supra,* did not affect plaintiffs' right to bring the case in the federal courts. But the District Court then upheld defendants' argument that since the tender offer had been thwarted, plaintiffs could not have acted in reliance on the alleged misstatements and omissions. Hence the District Court dismissed the complaint for lack of jurisdiction over the subject matter and for failure to state a claim for which relief can be granted.

D. *The Court of Appeals' Decision*

The Court of Appeals affirmed the District Court's decision in a Per Curiam opinion. The thrust of the opinion is that there could have been no reliance, since the tender offer was frustrated.

The Court of Appeals noted, despite its conclusion, that statements "made on the eve of a tender offer by target or tendering companies" were not "wholly outside the scope

of the Williams Act." Indeed, the Court stressed that such pre-tender offer activity had to be regulated, "[o]therwise, either party would be free to disseminate misinformation up to the effective date of the tender offer, thus defeating in substantial part, the very purpose of the Act—informed decision making by shareholders."

The Court of Appeals decided, in the face of its own language which seems to the contrary, that there was no jurisdiction because the tender offer was, ultimately, abandoned. The Court stated that had the tender offer been continued, then the defendants' statements, alleged in the complaint at bar, would be actionable under the Williams Act.

Reasons for Granting the Writ

The Court of Appeals Has Decided An Important Question Of Federal Law Which Has Not Been, But Should Be, Settled By This Court

Since the passage of the Williams Act in 1968, hundreds of tender offers (to purchase publicly traded shares) have been made. The purpose of the Williams Act is to ensure that shareholders have the opportunity to evaluate any tender offer and decide for themselves whether or not to accept. At bar, the stock of McGraw-Hill was trading on the New York Stock Exchange at $25 per share, when American Express announced it would pay $40 per share for all of McGraw-Hill's stock that was tendered. The defendants—incumbent management of McGraw-Hill—resisted the American Express announcement with such vehemence and material misstatements that American Express abandoned the offer, and the McGraw-Hill stock returned to its pre-tender offer price of $25 per share.

The very purpose of the Williams Act, however, is to protect shareholders faced with the claims and counter-

claims that are made when a hostile tender offer is announced. *Piper* v. *Chris-Craft Industries,* 430 U.S. 1 (1977); *Electronic Specialty Co.* v. *International Controls Corp.,* 409 F.2d 937 (2d Cir. 1969). At bar, the American Express offer, announced to the public by appropriate press releases and accompanied with the required Schedule 14D-1 filing with the Securities and Exchange Commission, was immediately denounced and vilified by defendants. In *Applied Digital Data Systems* v. *Milgo Electronic Corp.,* 425 F.Supp. 1145 (S.D.N.Y. 1977), the court (per Weinfeld, J.) recognized that the Williams Act would be hollow protection if its coverage did not include all misstatements made to defeat a tender offer. As the *Applied Digital* court held:

> "[To] confine the disclosure and fair-play provisions of the Act to the period after an offer has been formally made, would obviously frustrate the express remedial purposes of the statute. Indeed, it would be anomalous were sections 14(d) and 14(e) not applicable to the offeror or target corporation once a public announcement of an imminent tender or exchange offer was made, for numerous misstatements, omissions and half-truths could be promulgated with relative impunity until the offer was actually filed with and approved by the SEC. Although the shareholders might not in the pre-offer period be faced with a present decision whether to exchange their stock in the target corporation, statements and actions of the target corporation and the offeror during this period clearly have the capacity to affect any future decision and should thus fall within the purview of the statute." *Id.* at 1154.

This Court has not yet decided at what stage of a tender offer the protection of the Williams Act begins. If the decision in *Applied Digital* is correct—that the Act's pro-

tection must begin "once a public announcement of an imminent tender or exchange offer was made"—then this Court should make that protection clear. Until there is a definitive decision by this Court on when, exactly, during a tender offer struggle the protection of the Williams Act is triggered, there will be great confusion and doubt about the effectiveness of that law.

Hostile tender offers have become a permanent part of the business scene. The Court of Appeals, by narrowly restricting the Williams Act, has decided an important question of federal law which should be settled by this Court. For the Court of Appeals' decision withdraws Williams Act protection when it is needed most—from tender offers that are thwarted by material misstatements and manipulative acts. The Court of Appeals' decision will have the harmful and immediate effect of encouraging all sorts of irresponsible resistance to bona fide tender offers.

Williams Act protection affects millions of shareholders. This Court should review a case that imposes unwarranted restrictions on the Act's scope, in direct violation of the stated Congressional purpose.

CONCLUSION

For the reasons set forth above, Petitioners pray that a writ of certiorari issue to review the judgment of the Court of Appeals for the Second Circuit.

Dated: June 26, 1980

Respectfully submitted,

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APPENDIX

Appendix A

(Opinion of the United States Court of Appeals for the Second Circuit)

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

Nos. 953, 1101—September Term, 1979

(Argued March 26, 1980 Decided April 3, 1980)

Docket Nos. 79-7883, 80-7203

HARRY LEWIS, ALFRED B. REISS, CAROLA GRUEN, as Executrix of the estate of her late husband, Theodore Gruen, IRA BARMARK and COLONIAL SECURITIES CORPORATION,

Plaintiffs-Appellants,

—v.—

HAROLD W. MCGRAW, JR., JOHN L. MCGRAW, DANIEL F. CROWLEY, PETER O. LAWSON-JOHNSTON, KAY K. MAZUY, WILLIAM J. MCGILL, GORDON W. MCKINLEY, ALAN J. PIFER, LOUIS PUTZE, HOWARD S. TUTHILL, JAMES E. WEBB, VERNON R. ALDEN, GEORGE R. WEBSTER and MCGRAW-HILL, INC.,

Defendants-Appellees.

Appendix A

Before:

KAUFMAN, *Chief Judge,*
MESKILL, *Circuit Judge,*
and BRIEANT, *District Judge.**

Appeal from a judgment entered in the United States District Court for the Southern District of New York, Constance B. Motley, *District Judge,* dismissing appellant's complaint, brought under the Williams Act, 15 U.S.C. §78n(e) for failure to state a claim under Fed. R. Civ. P. 12.

Affirmed.

STUART D. WECHSLER, New York, New York (Robert I. Harwood, Mordecai Rosenfeld, A. Arnold Gershon, New York, New York, of counsel), *for Plaintiffs-Appellants.*

HERBERT M. WACHTELL, New York, New York (Douglas S. Liebhafsky, Michael W. Schwartz, Theodore N. Mirvis, of counsel), *for Defendants-Appellees.*

* Of the United States District Court for the Southern District of New York, sitting by designation.

Appendix A

PER CURIAM:

The instant action is a consolidation of five similar lawsuits brought on behalf of McGraw-Hill, Inc. stockholders, alleging that McGraw-Hill and its directors made false statements of material facts in response to two proposals of the American Express Company for the acquisition of substantial amounts of McGraw-Hill stock. The issue before us is whether shareholders may maintain a cause of action for damages under the Williams Act, 15 U.S.C. § 78n(e),[1] where they concede that no tender offer has been made to them. We conclude that they may not.

I

On January 8, 1979, American Express proposed to McGraw-Hill what plaintiff describes as a "friendly business combination" of the two companies through payment by American Express of $34 in cash for each McGraw-Hill share. Alternatively, American Express indicated its willingness to acquire 49% of McGraw-Hill's shares for cash or a combination of cash and securities. McGraw-Hill common stock was trading at $26 per share immediately prior to the announcement. On January 15, 1979, McGraw-Hill announced that its Board of Directors had rejected the proposal and made

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1 This section provides:

> It shall be unlawful for any person to make any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements made, in light of the circumstances under which they are made, not misleading, or to engage in any fraudulent, deceptive, or manipulative acts or practices, in connection with any tender offer or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any such offer, request, or invitation.

public a letter to American Express characterizing the offer as "reckless," "illegal," and "improper." The following day, American Express filed Schedule 14D-1 with the Securities and Exchange Commission concerning its intention to make a cash tender offer for any and all of McGraw-Hill's stock.

The proposed offer was never made, however, for on January 29, American Express retracted its earlier announcement, and in its place submitted a new proposal to the McGraw-Hill board. This offer, at a price of $40 per share, would not become effective unless McGraw-Hill's incumbent management agreed not to oppose it by "propaganda, lobbying, or litigation." The offer was rejected by the McGraw-Hill board two days later, and expired, by its own terms, on March 1.

Plaintiffs' consolidated, amended complaint charges that:

> Defendants announced publicly that the tender offer price of $40 per share was inadequate, although they knew that the price . . . was fair . . . .
>
> Defendants, in resisting the AMEXCO [American Express Company] tender offer [*sic*], challenged the integrity and honesty of AMEXCO (by indicating that AMEXCO had illegally complied with the Arab boycott), publicly challenged the legality of the tender offer (by indicating that the federal Bank Holding Company [Act] may preclude the tender offer), and publicly stated that the tender offer somehow threatened freedom of expression under the First Amendment of the Constitution (by stating that since the McGraw-Hill [*sic*] was engaged in publishing, its indepen-

dence would be smothered by a large financial institution such as AMEXCO).

These statements, as well as McGraw-Hill's characterization of the initial proposal as "reckless," "illegal," and "improper," are alleged to be false, as evidenced by the fact that, some months earlier, McGraw-Hill had advised American Express that it considered it to be a proper and desirable merger partner.

Plaintiffs concede that no tender offer ever took place—that no McGraw-Hill shareholder was ever in a position to offer his shares to American Express at a stated price. The $34 proposal was withdrawn before it became effective, and was replaced with a $40 proposal that could have ripened into an offer only upon the acquiescence of the McGraw-Hill board. Nonetheless, plaintiffs claim, "had defendants provided . . . shareholders and the public with complete and truthful information about AMEXCO and its proposed tender offer (*i.e.* that $40 per share was a fair price, and that AMEXCO was a company with which defendants themselves had wanted to merge), the AMEXCO tender offer would have been consummated." Accordingly, they each seek damages from the company and its directors for the difference between the $40 proposed tender price, and the $25 price to which the stock returned after the expiration of the American Express proposal.

Judge Motley dismissed the consolidated amended complaint pursuant to Fed. R. Civ. P. 12, noting that "plaintiffs fail to allege that McGraw-Hill stockholders, or anyone else for that matter, in fact relied upon the alleged misrepresentations or omissions. While plaintiffs do allege deception on the part of defendants,

plaintiffs do not allege that anyone was deceived or that anyone acted in reliance upon the alleged deception to their detriment." Having found plaintiffs' federal claim critically insufficient, the district court dismissed plaintiffs' pendent state claims for want of jurisdiction.

II

The complaint was properly dismissed. Section 14(e) of the Williams Act, 15 U.S.C. § 78n(e), has as its "sole purpose" the "protection of investors who are confronted with a tender offer." *Piper v. Chris-Craft Industries, Inc.*, 430 U.S. 1, 35 (1977). It is designed "to ensure that [investors] will not be required to respond [to a tender offer] without adequate information." *Rondeau v. Mosinee Paper Corp.*, 42 U.S. 49, 58 (1975). Accordingly, one element of a cause of action under § 14e is a showing "that there was misrepresentation upon which the target corporation shareholders *relied*." *Chris-Craft Industries, Inc. v. Piper Aircraft Corp.*, 480 F.2d 341 (2d Cir.), *cert. denied*, 414 U.S. 910 (1973) (emphasis supplied).[2] In the instant case, the target's

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2 We note that the element of reliance has been held "irrelevant" to a cause of action under Rule 10b-5, where material misstatements can be shown to have caused the issuance of securities which, in turn, resulted in losses to plaintiff purchasers. *Shores v. Sklar* [Current] CCH Fed. Sec. L. Rep. ¶ 97,252 at 96,770 (5th Cir. 1980). In *Shores*, plaintiffs could plausibly claim that if defendants had disclosed the truth concerning the financial condition of the issuer, the bond issue in question would never have been marketed. In the case at bar, by contrast, plaintiffs must contend that but for the alleged misstatements and omissions on the part of defendants, American Express would have proceeded with a hostile tender offer, over the opposition of McGraw-Hill. Such a scenario stretches the principle of causation into the realm of mere speculation, for it depends upon proof of an offer that, for all that appears here, American Express never even contemplated.

shareholders simply could not have relied upon McGraw-Hill's statements, whether true or false, since they were never given an opportunity to tender their shares.

Plaintiffs do not contest this indisputable fact, but rather rest upon cases holding that reliance may sometimes be presumed from a showing of materiality. *Mills v. Electric Auto-Lite Co.*, 396 U.S. 375 (1970); *Affiliated Ute Citizens v. United States*, 406 U.S. 128 (1972). These cases, however, in presuming reliance, did not abolish it as an element of the cause of action. Rather, they held that in cases in which reliance is possible, and even likely, but is unduly burdensome to prove, the resulting doubt would be resolved in favor of the class the statute was designed to protect. *Mills v. Electric Auto-Lite Co.*, *supra*, 396 U.S. at 385. We therefore presume reliance only "where it is logical" to do so. *Chris-Craft Industries, Inc. v. Piper Aircraft Corp.*, *supra*, 480 F.2d at 375. Here, where no reliance was possible under any imaginable set of facts, such a presumption would be illogical in the extreme.

We note in closing that our holding today does not place statements made on the eve of a tender offer by target or tendering companies wholly outside the scope of the Williams Act. On the contrary, where the offer ultimately becomes effective, and reliance can be demonstrated or presumed, such statements may well be made "in connection with a tender offer" as required by § 14e. Otherwise, either party would be free to disseminate misinformation up to the effective date of the tender offer, thus defeating in substantial part, the very purpose of the Act—informed decisionmaking by shareholders. Injunctive relief, moreover, may be available to restrain or correct misleading statements

made during the period preceding a tender offer where it appears that such an offer is likely, and that reliance upon the statements at issue is probable under the circumstances. *Applied Digital Data Systems, Inc. v. Milgo Electronic Corp.*, 425 F. Supp. 1145, 1154-55 (S.D.N.Y. 1977) (Weinfeld, J.). Finally, we must bear in mind that many of the wrongs alleged in this complaint may be recast as state law claims for breach of the fiduciary duties owed to shareholders by directors. *See Santa Fe Industries, Inc. v. Green*, 430 U.S. 462 (1977). Indeed, we note that several plaintiffs have commenced state court actions arising out of the abortive transactions at issue here. In this case, however, since American Express never made its proposed offer to the shareholders of McGraw-Hill, plaintiffs cannot state a cause of action for alleged misstatements under the Williams Act.

Appendix B

(Opinion of the United States District Court for the Southern District of New York)

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

79 Civ. 0552

HARRY LEWIS, ALFRED B. REISS, CAROLA GRUEN, as Executrix of the estate of her late husband, Theodore Gruen, IRA BARMAK and COLONIAL SECURITIES CORPORATION,

Plaintiffs,

—against—

HAROLD W. McGRAW, JR., JOHN L. McGRAW, DANIEL F. CROWLEY, PETER O. LAWSON-JOHNSTON, KAY K. MAZUY, WILLIAM J. McGILL, GORDON W. McKINLEY, ALAN J. PIFER, LOUIS PUTZE, HOWARD S. TUTHILL, JAMES E. WEBB, VERNON R. ALDEN, GEORGE R. WEBSTER and McGRAW-HILL, INC.,

Defendants.

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Appendix B

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CONSTANCE BAKER MOTLEY, *D. J.*

MEMORANDUM OPINION

Defendants in this action have moved for an order, pursuant to Rules 12(b)(1) and 12(b)(6) of the Federal Rules of Civil Procedure, dismissing the complaint for lack of jurisdiction over the subject matter and/or for failure of the federal claims alleged to state a claim upon which relief can be granted. Defendants also have moved, in the alternative, for an order staying the action pending disposition of parallel state-court actions.

The five named plaintiffs originally commenced separate class actions against the defendants. Following defendants' motion to dismiss each of the five complaints, plaintiffs served and filed a consolidated amended complaint. By stipulation among all parties, defendants' motion to dismiss was deemed addressed to the new complaint.

Plaintiffs, shareholders of defendant McGraw-Hill, Inc. (McGraw-Hill), allege in their consolidated amended complaint that defendants violated Section 14(e) of the Securities Exchange Act of 1934, as amended, 15 U.S.C. § 78n(e), in connection with a proposed tender offer by the American Express Company (AMEXCO) for the common stock of McGraw-Hill. The individual defendants in this action are

directors of McGraw-Hill. The series of events leading to the alleged violation of Section 14(e) began on January 8, 1979, when AMEXCO publicly proposed to McGraw-Hill a friendly business combination on the basis of AMEXCO's acquisition of 49% of McGraw-Hill's outstanding securities at $34 per share. Plaintiffs allege that the price per share initially offered by AMEXCO was a substantial premium over $26, the market price of the common stock prior to the proposed AMEXCO offer. Soon thereafter AMEXCO increased its proposed offer to $40 per share for all of McGraw-Hill's shares. In connection with these proposed offers, AMEXCO filed a Schedule 14D-1 with the Securities and Exchange Commission.

Plaintiffs allege that defendants refused to negotiate with AMEXCO and "embarked on an unlawful, improper and illegal plan, scheme and conspiracy to obstruct, delay and defeat the proposed AMEXCO offer." In particular, plaintiffs allege that defendants made untrue statements of material facts and omitted to state material facts, and engaged in fraudulent and deceptive acts and practices, as follows:

1) Defendants announced that the proposed tender offer price of $40 per share was inadequate, although they allegedly knew that the price was fair. Plaintiffs allege that defendants had no genuine basis for believing that the McGraw-Hill stock was worth more than $40 per share.

2) Plaintiffs allege that defendants challenged the integrity and honesty of AMEXCO, publicly challenged the legality of the proposed tender offer, and publicly stated that the proposed tender offer somehow threatened freedom of expression. Plaintiffs maintain that these statements were false and misleading, especially since defendants omitted to advise its shareholders that McGraw-Hill had

earlier advised AMEXCO that McGraw-Hill considered AMEXCO to be a proper and desirable merger partner.

3) Plaintiffs allege that defendants circulated a letter which McGraw-Hill had sent to AMEXCO, characterizing the proposed merger as "reckless," "illegal," and "improper."

4) Plaintiffs allege that defendants denied the plaintiff class the opportunity to sell their McGraw-Hill stock at a large premium.

Plaintiffs allege that the tender offer would have been consummated had defendants provided its shareholders and the public with complete and truthful information about AMEXCO and its proposed tender offer. Instead, defendants rejected the AMEXCO $40 per share proposed offer on January 31, 1979. Plaintiffs allege that defendants violated their statutory and common law fiduciary duties by thwarting the proposed AMEXCO tender offer improperly and illegally.

Conduct "In Connection With" A Tender Offer

Section 14(e) provides:

> It shall be unlawful for any person to make any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, or to engage in any fraudulent, deceptive, or manipulative acts or practices, in connection with any tender offer or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any such offer, request, or invitation.

Appendix B

The sole purpose of the Williams Act of 1968, which added Section 14(e), "was the protection of investors who are confronted with a tender offer." *Piper* v. *Chris-Craft Industries, Inc.*, 430 U.S. 1, 35 (1977). Thus, "'[t]he purpose of the Williams Act is to insure that public shareholders who are confronted by a cash tender offer for their stock will not be required to respond without adequate information.'" *Id.* (quoting *Rondeau* v. *Mosinee Paper Corp.*, 422 U.S. 49, 58 (1975)).

The Supreme Court has repeatedly cautioned that "[t]he starting point in every case involving construction of a statute is the language itself." *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 756 (1975) (Powell, J., concurring), *quoted in Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 197 (1976). The critical phrase in Section 14(e) is "in connection with any tender offer." The issue is whether or not the conduct alleged by plaintiffs to have violate [*sic*] Section 14(e) was "in connection with any tender offer." In the case at hand, it appears indisputable that no tender offer ever existed; all that occurred was a "proposed" tender offer by AMEXCO.

The standards to be applied in determining whether conduct is "in connection with a tender offer" were set forth by this court in *Applied Digital Data Systems, Inc.* v. *Milgo Electronic Corp.*, 425 F. Supp. 1145 (S.D.N.Y. 1977). The court in *Applied Digital* held that when "a public announcement of a proposed offer has been made, the very dangers that the Act was intended to guard against come into play, and the application of sections 14(d) and 14(e) is thus appropriate." *Id.* at 1155 [footnote omitted]. The court explained that "[t]here is no apparent reason why any given action may not be taken 'in connection with' a development reasonably certain to take place in the future

or why a recommendation to reject a proposed tender offer is not also a recommendation to 'reject a tender offer.'" *Id.* at 1153. In a critical passage, the *Applied Digital* court reasoned that:

> [To] confine the disclosure and fair-play provisions of the Act to the period after an offer has been formally made, would obviously frustrate the express remedial purposes of the statute. Indeed, it would be anomalous were sections 14(d) and 14(e) not applicable to the offeror or target corporation once a public announcement of an imminent tender or exchange offer was made, for numerous misstatements, omissions and half-truths could be promulgated with relative impunity until the offer was actually filed with and approved by the SEC. Although the shareholders might not in the pre-offer period be faced with a present decision whether to exchange their stock in the target corporation, statements and actions of the target corporation and offeror during this period clearly have the capacity to affect any future decision and should thus fall within the purview of the statute.

Id. at 1154 [footnote omitted].

This court has subsequently indicated that *Applied Digital* allows a Section 14(e) action only where the prospective offeror has made a public announcement of a proposed tender offer and has established a clear and definite intent to make a tender offer. *Reserve Management Corp.* v. *Anchor Daily Income Fund, Inc.*, 459 F. Supp. 597, 608 (S.D.N.Y. 1978). In the case at hand, the facts, as alleged by plaintiffs, suggest that AMEXCO had indeed made a public announcement of its proposed tender offer. More-

over, the facts alleged by plaintiffs appear sufficient to establish a clear and definite intent on the part of AMEXCO to make a tender offer. Plaintiffs have alleged statements and actions by defendants which clearly would have had the capacity to affect any future decision by stockholders in a tender offer. Thus, Section 14(e) should apply to statements and actions made by defendants.

Defendants suggest that the doctrine of *Applied Digital* should be limited to only those cases where injunctive relief is sought in the face of an immediate and threatened tender offer. This court finds this argument unpersuasive; nothing in the *Applied Digital* opinion suggests that its reasoning should be limited to actions for injunctive relief. Moreover, it would be inconsistent with the purpose of Section 14(e) to preclude an action for damages relating to pre-tender offer violations in cases where no tender offer was in fact made. Such a limitation of *Applied Digital* would have the effect of providing a safe harbor for target companies who were successful in their use of misstatements or deception to discourage the making of tender offers.

In summary, the court finds that plaintiffs have alleged conduct "in connection with" a tender offer under Section 14(e).

Santa Fe Industries, Inc. v. *Green*

Defendants argue that the consolidated amended complaint alleges only breaches of fiduciary duty, and that the complaint fails to allege actionable deception under the principles of *Santa Fe Industries, Inc.* v. *Green,* 430 U.S. 462 (1977). In *Santa Fe Industries,* the Supreme Court held that a claim "states a cause of action under any part of the Rule 10b-5 only if the conduct alleged can be fairly

viewed as 'manipulative or deceptive' within the meaning of the statute." *Id.* at 473-74. The principles of *Santa Fe Industries* apply to claims under Section 14(e) as well as Section 10(b). *Marshel* v. *AFW Fabric Corp.*, 441 F. Supp. 299, 300 (S.D.N.Y. 1977); *Altman* v. *Knight*, 431 F. Supp. 309, 313-14 (S.D.N.Y. 1977).

This court has recently recognized, however, that:

> The Court's holding in *Santa Fe Industries* makes a showing of manipulation or deception a requirement in a Rule 10b-5 action, but does not, as defendants seemingly maintain, bar all claims related to breaches of fiduciary duty under state law. As the Second Circuit explained in *Goldberg* v. *Meridor*, 567 F.2d 209, 221 (2d Cir. 1977), *cert. denied*, 434 U.S. 1069 (1978), in *Santa Fe Industries* the Supreme Court was "drawing the line so as to require plaintiffs to make claims of nondisclosure or misleading disclosure, not as directing the lower courts to dismiss cases where it was claimed that fiduciaries had failed to disclose their self-dealing or had made a misleading disclosure." . . . Where, as here, breaches of fiduciary duty may also involve manipulation or deception, a plaintiff may advance claims under both Rule 10b-5 and state law.

Jones v. *National Distillers and Chemical Corp.*, [Current] Fed. Sec. L. Rep. (CCH) ¶ 97,140, at 96,293-94 (S.D.N.Y. Oct. 10, 1979). These principles are equally applicable in the context of a Section 14(e) action.

In the case at hand, plaintiffs allege that defendants made misleading disclosures: 1) by announcing that the proposed tender offer price of $40 per share was inadequate; 2) by circulating a letter characterizing the pro-

posed merger as "reckless," "illegal," and "improper"; and 3) by challenging the integrity and honesty of AMEXCO, as well as the legality of the proposed tender offer. In addition plaintiffs allege that defendants failed to disclose that McGraw-Hill had previously advised AMEXCO that McGraw-Hill considered AMEXCO to be a proper and desirable merger partner. As plaintiffs have clearly made claims of both nondisclosure and misleading disclosure, the principles of *Santa Fe Industries* do not require dismissal of this case. While plaintiffs' claims may involve breaches of fiduciary duty, their claims involve nondisclosure and misleading disclosures as well. Thus, the alleged conduct of defendants can fairly be viewed as manipulative or deceptive within the meaning of Section 14(e).

Defendants cite a number of cases in which breaches of fiduciary duty were held not to be actionable under federal securities law. In particular, defendants refer to cases involving "bootstrap" allegations, that is, where plaintiffs allege failure to disclose an alleged breach of fiduciary duty. For example, in *Browning Debenture Holders' Committee* v. *DASA Corp.*, 560 F.2d 1078, 1084 (2d Cir. 1977), the Second Circuit stated that "violation of any such state-law fiduciary duties, including non-disclosure of conflict of interest or unfairness of a conversion price, will not support a claim of constructive fraud under §14(a)." This court has recently noted, however, that "in *Brown*, as in other cases cited by defendants, the court addressed the situation where there was no deception or material misstatements or omission, and did not require dismissal of an action where plaintiff did allege deception or material misstatement or omission accompanying the alleged breach of fiduciary duty." *Jones* v. *National Distillers and Chemical Corp.*, *supra*, at 96,294. In the case at hand, plaintiff

alleges a number of misstatements and omissions which are not of the "bootstrap" variety merely alleging failure to disclose a breach of fiduciary duty.

Defendants argue that the court's recent decision in *In re Sunshine Mining Co. Securities Litigation,* 77 Civ. 4020 (S.D.N.Y. May 25, 1979), is "virtually 'on all fours'" with the case at hand. In *Sunshine Mining,* the court held that the wrongful withholding of support for a proposed tender offer does not amount to a fraudulent, deceptive, or manipulative act or practice under the principles of *Santa Fe Industries.* The court explained that "[s]ince plaintiff's claim that approval of the tender offer was withheld by management for purely selfish reasons amounts to no more than a charge that Sunshine management acted unfairly and in breach of its fiduciary duties, plaintiff does not state a cause of action under the federal securities laws." Slip op. at 6. In the case at hand, unlike in *Sunshine Mining,* plaintiff alleges misstatements and omissions actionable under Section 14(e). Thus, it is clear that neither *Santa Fe Industries* nor any of the other cases cited by defendants on this point require dismissal of the consolidated amended complaint.

Causation and Reliance

It is well-established that in a Section 14(e) action, plaintiffs "must show that there was a misrepresentation upon which the target corporation stockholders relied and that this was in fact the cause of [plaintiffs'] injury." *Chris-Craft Industries, Inc.* v. *Piper Aircraft Corp.,* 480 F.2d 341, 373 (2d Cir.), *cert. denied,* 414 U.S. 910 (1973). In the case at hand, it would appear that plaintiffs fail to allege that McGraw-Hill stockholders, or anyone else for

that matter, in fact relied upon the alleged misrepresentations or omissions. While plaintiffs do allege deception on the part of defendants, plaintiffs do not allege that anyone was deceived or that anyone acted in reliance upon the alleged deception to their detriment. This court recently stressed the importance of alleging reliance and causation in the Section 10(b) context:

> [B]efore the court can ask "Was the conduct deceptive?", it must first ascertain "To whom?" Since a 10b-5 action requires a causal connection between the defendant's violation and the plaintiff's loss, the allegedly deceived observers will have to be persons who were in a position to make a decision that led to that loss.

Klamberg v. *Roth,* 473 F. Supp. 544, 550 (S.D.N.Y. 1979) [footnote omitted].

In the case at hand, plaintiffs, as stockholders, were simply never in a position to make a decision that could lead to any loss. The only attempt to allege reliance or causation in the consolidated amended complaint is its allegation that:

> Had defendants provided its shareholders and the public with complete and truthful information about AMEXCO and its proposed tender offer (i.e., that $40 per share was a fair price; and that AMEXCO was a company with which defendants themselves had wanted to merge), the AMEXCO tender offer would have been consummated.

A similar allegation was held insufficient by this court in *Rediker* v. *Geon Industries, Inc.,* 464 F. Supp. 73 (S.D. N.Y. 1978). In *Rediker,* the plaintiff alleged that the de-

fendant executives of Geon had engaged in fraudulent activities as a result of which Burmah, an intended tendering party, had determined to desist from going forward with the deal. The court held:

> Plaintiff must show that there was a misrepresentation upon which she and other target shareholders relied and that this reliance was in fact the cause of their injury. . . . The facts as alleged herein do not establish that Geon shareholders' reliance on the alleged misrepresentation was the cause of the shareholders' injury. Misdeeds by the defendants may have caused Burmah to abort the deal, and this, in turn, may have caused the market price of Geon to plummet and may have thereby injured plaintiffs. Thus, the alleged injury was caused by the aborting of the deal and not by the shareholders' reliance on defendants' alleged misrepresentations. Plaintiff's remedies, if any, lie in state court for common law claims.

Id. at 82 [footnote and citations omitted]. *See also Hundahl* v. *United Benefit Life Insurance Co.*, 465 F. Supp. 1349, 1366-70 (N.D. Tex. 1979); *Halle & Stieglitz, Filor, Bullard Inc.* v. *Empress International, Ltd.*, 442 F. Supp. 217, 225 (D. Del. 1977); *Altman* v. *Knight, supra,* at 314.

Here, as in *Rediker,* plaintiff alleges that defendants have frustrated the consummation of a tender offer. Such a theory will not support a Section 14(e) action. Plaintiffs allege neither reliance on the part of stockholders nor reliance on the part of AMEXCO—in fact, any suggestion that AMEXCO withdrew its proposed tender offer in *reliance* upon the alleged McGraw-Hill misrepresentations and omissions would be absurd. Even assuming that misrepresentations or omissions thwarted the proposed

AMEXCO tender offer, such an allegation would not give rise to a Section 14(e) violation. The situation is not unlike that in *Blue Chip Stamps* v. *Manor Drug Stores, supra,* where the Supreme Court held that fraudulent misrepresentations which prevented a "purchase" of a security from ever taking place did not give rise to a violation of Rule 10b-5.

Of course, this court recognizes that in many circumstances a presumption of reliance and causation may be triggered by a finding of materiality. *See Affiliated Ute Citizens* v. *United States,* 406 U.S. 128, 153-54 (1972); *Mills* v. *Electric Auto-Lite Co.,* 396 U.S. 375, 385 (1970); *Chris-Craft Industries, Inc.* v. *Piper Aircraft Corp.,* 480 F.2d 341, 375 (2d Cir.), *cert. denied,* 414 U.S. 910 (1973). In the case at hand, however, such a presumption would be totally inappropriate. As discussed above, not only have plaintiffs failed to allege reliance on the part of stockholders, but also the facts as alleged by plaintiffs present a situation in which reliance was virtually impossible. As no tender offer was ever actually made by AMEXCO to McGraw-Hill stockholders, these stockholders were never in a position to rely upon the alleged misstatements or omissions by McGraw-Hill. This is not to say that reliance upon pre-tender offer misstatements and omissions is precluded in all cases. This court holds, however, that plaintiffs' consolidated amended complaint must be dismissed for failure to allege reliance and causation in a manner sufficient to sustain its Section 14(e) claim.

State Claim

Upon dismissal of plaintiffs' federal claim, their state-law claim of breach of fiduciary duty also must be dismissed for lack of pendant [*sic*] jurisdiction. The Supreme Court

has instructed that "if the federal claims are dismissed before trial, even though not insubstantial in a jurisdictional sense, the state claims should be dismissed as well." *United Mine Workers* v. *Gibbs,* 383 U.S. 715, 726 (1966); *accord, Kavit* v. *A. L. Stamm & Co.,* 491 F.2d 1176, 1179 (2d Cir. 1974). "Pendent jurisdiction can be relied upon only where there is a claim conferring federal jurisdiction that will survive a motion to dismiss." *IIT* v. *Vencap, Ltd.,* 519 F.2d 1001, 1015 (2d Cir. 1975).

Conclusion

For the reasons stated above, defendants' motion to dismiss the complaint for lack of jurisdiction over the subject matter and for failure to state a claim for which relief can be granted must be granted. Accordingly, it is not necessary for the court to address defendants' motion for a stay.

Dated: New York, New York
November 30, 1979

So Ordered.

Constance Baker Motley
U.S.D.J.

No. 79-2054

Supreme Court, U. S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

HARRY LEWIS, ALFRED B. REISS, CAROLA GRUEN, as Executrix of the estate of her late husband, Theodore Gruen, IRA BARMAK and COLONIAL SECURITIES CORPORATION,

Petitioners,

v.

HAROLD W. MCGRAW, JR., JOHN L. MCGRAW, DANIEL F. CROWLEY, PETER O. LAWSON-JOHNSTON, KAY K. MAZUY, WILLIAM J. MCGILL, GORDON W. MCKINLEY, ALAN J. PIFER, LOUIS PUTZE, HAROLD S. TUTHILL, JAMES E. WEBB, VERNON R. ALDEN, GEORGE R. WEBSTER and MCGRAW-HILL, INC.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM IN RESPONSE TO PETITION FOR A WRIT OF CERTIORARI

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No. 79-2054

IN THE

Supreme Court of the United States

OCTOBER TERM, 1980

HARRY LEWIS, ALFRED B. REISS, CAROLA GRUEN, as Executrix of the estate of her late husband, Theodore Gruen, IRA BARMAK and COLONIAL SECURITIES CORPORATION,

Petitioners,

v.

HAROLD W. MCGRAW, JR., JOHN L. MCGRAW, DANIEL F. CROWLEY, PETER O. LAWSON-JOHNSTON, KAY K. MAZUY, WILLIAM J. MCGILL, GORDON W. MCKINLEY, ALAN J. PIFER, LOUIS PUTZE, HAROLD S. TUTHILL, JAMES E. WEBB, VERNON R. ALDEN, GEORGE R. WEBSTER and MCGRAW-HILL, INC.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

MEMORANDUM IN RESPONSE TO PETITION FOR A WRIT OF CERTIORARI

Preliminary Statement

Petitioners seek certiorari to review the judgment of the United States Court of Appeals for the Second Circuit which affirmed an Order and Judgment of the United States District Court for the Southern District of New York, Honorable

Constance Baker Motley, District Judge, dismissing consolidated actions for lack of subject matter jurisdiction and for failure to state a federal claim. The actions, brought against respondent McGraw-Hill, Inc. ("McGraw-Hill") and its directors, the individual respondents, sought damages on behalf of an asserted class of McGraw-Hill shareholders by virtue of respondents' rejection of a proposed tender offer by American Express Company ("Amexco") for all of the stock of McGraw-Hill. The proposed tender offer was abandoned by Amexco without ever having commenced. The action was purported to be based upon Section 14(e) of the Securities Exchange Act of 1934 with pendent claims that respondents allegedly breached common-law fiduciary duties to the class in rejecting the Amexco proposals.

Respondents choose to take no position as to whether this Court should grant certiorari in this matter.* Respondents did not originally submit a response to the certiorari petition. By letter dated September 11, 1980, the Clerk of this Court notified respondents' counsel that the Court had directed that a request be made of respondents to file a response. In compliance with that request, respondents respectfully submit the present memorandum which will endeavor to set forth factors which this Court may deem germane to its determination as to whether or not to grant certiorari.

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* There are presently pending in the New York State Supreme Court, New York County, four consolidated class actions—three brought by the same plaintiffs as commenced the actions below—which essentially duplicate the claims asserted against respondents in the District Court. Plaintiffs in the state-court action are represented by the same lead counsel as appears for plaintiffs in the federal courts. By stipulation among the parties, all proceedings in the state-court actions have essentially been stayed pending final determination by the federal courts of respondents' dismissal motion. Thus, a grant of certiorari by this Court would effectively operate to continue the present stay of the New York state-court actions.

QUESTIONS PRESENTED

Respondents submit that the "question presented" by petitioners should be restated as follows:

1. Did the Court of Appeals correctly hold that shareholders of a target company could not maintain a cause of action for damages under the Williams Act, Section 14(e), where it is conceded that no tender offer was ever made, that the shareholders were never confronted with an investment decision as to whether or not to tender their shares, and that the shareholders never relied upon the "deceptions" alleged?* See Point I *infra*.

Were certiorari to be granted herein, respondents (in supporting the judgment under review) would tender the following additional questions for resolution by the Court:

2. Can this Court's holding in *Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462, 477 (1977), that the fraud provisions of the Securities Exchange Act (there Section 10(b) and Rule 10b-5) do not reach cases "in which the essence of the complaint is that shareholders were treated unfairly by a fiduciary" be circumvented by inclusion in a federal court complaint of "bootstrap" allegations of "fraud" consisting in essence of nothing more than a claim that defendants failed to disclose their supposed breach of fiduciary duties? See Point II *infra*.

3. Does Section 14(e) give rise to *any* implied private cause of action for damages? See Point III *infra*.

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* Petitioners' "question presented" (Petition, p. 2) imputes "manipulative" practices to respondents as well. Petitioners' complaint (*quoted in Lewis* v. *McGraw*, 619 F.2d 192, 194 (2d Cir. 1980)), however, alleges no conduct which could conceivably qualify as "manipulative" within this Court's decisions. See *Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462, 476-77 (1977); *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 199 & n.21 (1976).

STATEMENT OF THE CASE

Respondents believe that a brief review of the nature of the case and the prior proceedings—both state and federal—would be helpful to this Court in placing in context the issues raised by the certiorari petition.

A. The Amexco takeover proposals.

The actions below arose out of two takeover proposals for McGraw-Hill made by Amexco in early 1979. The first consisted of a proposed "hostile" takeover by Amexco, which announced its intention on January 16, 1979 to make a tender offer to McGraw-Hill shareholders at a price of $34 per share. This proposed tender offer was unanimously determined by the McGraw-Hill Board of Directors to be grossly inadequate in price, to raise serious legal questions, and to be contrary to the best interests of McGraw-Hill and its shareholders.*

The Amexco proposed tender offer accordingly came under litigation challenge by McGraw-Hill both in the United States District Court for the Southern District of New York and in the New York State Supreme Court. In addition, the proposed acquisition of McGraw-Hill—a major American publishing, journalism, broadcasting and financial information company—by an international financial and banking institution such as Amexco was met with widespread opposition in the press and from authors, editors and customers upon whom McGraw-Hill was dependent for its business existence. The proposed transaction also came under scrutiny from concerned governmental agencies, including the Federal Trade Commission.

On January 29, 1979, Amexco withdrew its $34 proposal for McGraw-Hill, only minutes before deposition testimony of key Amexco executives was to commence. In its place,

---

* By virtue of a state-court preliminary injunction motion made and then withdrawn by plaintiff shareholders, see pp. 6-8 *infra*, a detailed evidentiary showing was made of record by respondents of the facts that transpired in this matter.

Amexco announced a new plan—a "friendly" proposed tender offer for McGraw-Hill at $40 per share conditioned, however, upon the McGraw-Hill Board of Directors' either recommending the proposal or interposing no opposition whatsoever "by propaganda, lobbying, litigation or otherwise."

The revised Amexco proposal received careful consideration from the Board of Directors of McGraw-Hill, which unanimously determined that it was financially inadequate, legally dubious and uncertain of consummation.

Subsequent to this rejection of its "friendly" proposal, Amexco announced that it would leave its proposal "open" until March 1, 1979, the stated premise being that McGraw-Hill might change its mind. The proposal then was permitted to expire on March 1.

B. The state and federal court actions.

The directors' determinations were challenged in a series of purported class actions by the present petitioners and others. The initial action was brought by petitioner Lewis in New York State Supreme Court and was followed two weeks later by an action in the District Court by the same petitioner, alleging not only state-law claims but a Section 14(e) claim as well. The *Lewis* actions were then followed by successive actions in state court and in the District Court below by the other petitioners.

All of the complaints, state and federal, sought to hold the director-respondents liable in damages charging that they had violated their state-law fiduciary duties by rejecting the Amexco proposals, by actively opposing them, and by not negotiating to sell McGraw-Hill to Amexco. The federal-court complaints also alleged that the directors had violated Section 14(e) of the Securities Exchange Act by virtue of allegedly "fraudulent" misstatements. Certain of the state-court complaints contain rather similar claims of common-law fraud.

C. Plaintiffs' preliminary injunction motion in the state court.

On February 9, 1979, while the second, "friendly" Amexco proposal was still open, a motion for a "preliminary mandatory injunction" on behalf of the class of McGraw-Hill shareholders was brought on in state court by order to show cause, seeking in substance to compel the defendant directors to accept the Amexco "friendly" $40 per share proposed transaction.

Defendants filed full answering papers—a comprehensive affidavit, documentary exhibits and a memorandum of law—demonstrating beyond doubt that the motion (and, indeed, the underlying action as well) was without either legal or factual merit. Thus, on the motion, defendants showed that the McGraw-Hill Board consisted overwhelmingly of distinguished, independent, "outside" directors in no way beholden to McGraw-Hill's management. It was further set forth that the Board had acted only after receiving expert advice from an independent investment banking firm and two outside law firms. And defendants made a detailed evidentiary showing that, after exhaustive consideration, the directors had unanimously determined in their reasonable business judgment that to consent to the Amexco proposal would be contrary to the best interests of McGraw-Hill and its stockholders for a number of reasons, the principal ones being:

— The Board had received independent investment banking advice from the firm of Morgan Stanley & Co., Inc., that, because the future prospects of McGraw-Hill as an independent entity were extremely bright and it was likely to experience excellent growth and market acceptance in the 1980s, it was not the appropriate time to sell or merge McGraw-Hill;

— The Board had received Morgan Stanley's considered opinion that the $40 price at which Amexco was making its proposal was an inadequate one for a sale of the enterprise even were it desired that

McGraw-Hill be sold at that time, and that a higher price could be obtained from others;

— The Board had received independent legal advice from two outside law firms that, in light of the serious questions of illegality raised by an Amexco/McGraw-Hill combination, any Amexco tender offer for McGraw-Hill—even if not opposed by McGraw-Hill—was virtually certain of being long delayed by governmental agencies with strong likelihood of ultimate withdrawal or prohibition; and

— The Board had concluded that, given the nature of McGraw-Hill's business, there was a grave risk that McGraw-Hill would be seriously damaged during the interim period of uncertainty as to the future of the company and that if, as anticipated, the Amexco offer ultimately failed of consummation, the shareholders would not only *not* receive the $40 price, but would be left owning "damaged goods."

In sum, it was shown in opposition to the state-court injunction motion that the Board had concluded that to accept the Amexco proposal was to place McGraw-Hill's business at risk of serious damage during what promised to be a lengthy and likely futile quest to obtain an inadequate price.*

The state-court motion initially came on to be heard before a Justice of the Supreme Court on February 22, 1979. In the face of the overwhelming evidentiary showing submitted by

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* The accuracy of the Board's conclusion that the $40 price being proposed in early 1979 by Amexco for a takeover of McGraw-Hill was inadequate has been borne out by subsequent events. As set forth by petitioners, prior to the initial Amexco proposal, McGraw-Hill shares had been trading at approximately $25 per share. As this brief is being written in October 1980, McGraw-Hill shares were trading at $39-7/8 in ordinary market transactions upon the New York Stock Exchange, *Wall Street Journal*, Oct. 7, 1980, at 52, col. 5, and were it deemed appropriate to sell the enterprise as a whole, a markedly higher takeover price would be readily obtainable.

defendants in their answering papers, plaintiffs chose to withdraw the motion rather than permit it to be heard by the state court.

D. Respondents' motion in the District Court.

Respondents moved the District Court to dismiss petitioners' Consolidated Amended Complaint. The basis of the motion was that the complaint failed to state a claim cognizable under Section 14(e) and that, federal jurisdiction being absent, the pendent state-law claims were likewise required to be dismissed.

In support of their motion below, respondents set forth for the District Court that:

1. The essence of petitioners' complaint was nothing more than a claim of supposed breach by respondents of their state-law fiduciary duties as directors, which claim was not cognizable by a federal court under *Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462 (1977), notwithstanding petitioners' "bootstrap" allegations of "deception" designed to circumvent the holding of *Santa Fe*;

2. Petitioners had not, and could not, allege that they (or anyone else) had relied upon any "misrepresentations" to their detriment: petitioners' "deception" allegations thus floated weightless in a vacuum neither relied upon nor causal of any "damages"; and

3. The proposed Amexco tender offer having been withdrawn by Amexco before it ever commenced, petitioners necessarily were unable to satisfy Section 14(e)'s requirement that the conduct for which they sought damages had occurred "in connection with" a tender offer.

By Memorandum Opinion and Order filed November 30, 1979, Judge Motley of the Southern District of New York granted respondents' motion to dismiss. *Lewis* v. *McGraw*,

[1979-80 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 97,195 (S.D.N.Y. 1979). In her opinion, Judge Motley expressly rejected respondents' "*Santa Fe*" and "in connection with" positions. *Id.* at 96,567-69. Judge Motley nevertheless agreed with respondents that petitioners' complaint was fatally defective in failing to allege reliance and causation as required under Section 14(e). *Id.* at 96,570. Judge Motley held:

> While plaintiffs do allege deception on the part of defendants, plaintiffs do not allege that anyone was deceived or that anyone acted in reliance upon the alleged deception to their detriment. . . .
>
> . . . .
>
> . . . Plaintiffs allege neither reliance on the part of stockholders nor reliance on the part of AMEXCO—in fact, any suggestion that AMEXCO withdrew its proposed tender offer in *reliance* upon the alleged McGraw-Hill misrepresentations and omissions would be absurd. Even assuming that misrepresentations or omissions thwarted the proposed AMEXCO tender offer, such an allegation would not give rise to a Section 14(e) violation.
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> *Id.* (emphasis in original).

E. Petitioners' appeal to the Second Circuit.

Petitioners took appeal to the Second Circuit from the District Court's dismissal of the action. Respondents in the Second Circuit relied upon all of the grounds for dismissal previously urged before the District Court. Respondents also "noted in passing" to the Second Circuit that recent decisions of this Court strongly suggest that no damage action of any kind is necessarily implicit in Section 14(e). The appeal came on before then Chief Judge Kaufman, Circuit Judge Meskill and District Judge Brieant, sitting by designation.

The Second Circuit on April 3, 1980, unanimously affirmed the District Court's determination. *Lewis* v. *McGraw*, 619 F.2d 192 (2d Cir. 1980) (per curiam). The Court of Appeals

agreed with the District Court that—in light of the conceded fact that no tender offer ever took place and no McGraw-Hill shareholder was ever in a position to offer his shares to Amexco—"the target's shareholders simply could not have relied upon McGraw-Hill's statements, whether true or false, since they were never given an opportunity to tender their shares", and that "no reliance was possible under any imaginable set of facts." *Id.* at 195. The Court of Appeals' opinion also appears to accept respondents' argument that, in the context of an after-the-fact suit for money damages where no tender offer has ever taken place, petitioners cannot satisfy the "in connection with any tender offer" requirement of Section 14(e). See *id.* and 15n.* *infra*. The Second Circuit indicated, however, that in its view the "in connection with" requirement *could* be satisfied in cases posing hypothetical factual circumstances not presented by the case at bar: (a) actions seeking pre-tender offer *injunctive* relief; and (b) actions seeking money damages on account of pre-tender offer fraudulent conduct where the offer ultimately *does* become effective and the fraudulent conduct can be found to have impacted the subsequent decision-making by shareholders. *Id.*

DISCUSSION

POINT I

The Second Circuit's decision is clearly correct and is in full accord with the decisions of this Court.

Petitioners urge that certiorari should be granted herein because this Court "has not yet decided at what stage of a tender offer the protection of the Williams Act begins." (Petition, p. 7.) Respondents agree that this precise issue has never been determined by this Court.

Nevertheless, it is submitted that the decision of the Court of Appeals is in full accord with prior precedents of this Court interpreting the various provisions of the securities laws and is likewise in full conformity with holdings of other Courts of Appeals as well as District Courts.

Indeed, the Second Circuit could not have reached any other conclusion in this matter without contravening any number of this Court's prior rulings as well as authoritative precedents of the lower federal courts:

1. This Court's *Chris-Craft* decision.

In *Piper* v. *Chris-Craft Industries, Inc.*, 430 U.S. 1, 35 (1977), after carefully reviewing the language and history of the Williams Act, this Court held:

> [T]he *sole* purpose of the Williams Act was the protection of investors *who are confronted with a tender offer.* As we stated in *Rondeau* v. *Mosinee Paper Corp.* [422 U.S. 49, 58 (1975)]: "The purpose of the Williams Act is to insure that public shareholders who are confronted by a cash tender offer for their stock will not be required to respond without adequate information . . . ."
>
> (Emphasis supplied.)

The legislative history of Section 14(e) is precisely to the same effect: the statute protects shareholders, but *only* those shareholders who must decide whether or not to tender.* In *Chris-Craft*, on the facts there presented, this Court held that Chris-Craft—although a shareholder of a company subject to an actual tender offer—had no "implied" Section 14(e) damage claim because it was confronted with no tender offer investment decision. As this Court explained:

> As a tender offeror actively engaged in competing for Piper stock, *Chris-Craft was not in the posture of a target shareholder confronted with the decision of whether to tender or retain his stock.* Consequently, Chris-Craft could scarcely have alleged a need for the disclosures mandated by the Williams Act. In short, the fact that Chris-Craft necessarily acquired Piper stock as a means of taking over Piper adds nothing to its § 14(e) standing arguments.
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> *Id.* at 35-36 (emphasis supplied; footnote omitted).

Since it is a given in the case at bar that the proposed Amexco tender offer for McGraw-Hill never in fact eventuated, the present petitioners were no more faced with a tender offer investment decision than was Chris-Craft; under this Court's reading of Section 14(e), then, it is submitted that petitioners can no more have a Section 14(e) damage claim than did Chris-Craft.

2. The lack of any reliance.

As the Second Circuit correctly pointed out—and petitioners have never disputed—"one element of a cause of action under § 14(e) is a showing 'that there was misrepresentation upon

* The legislative history is replete with statements emphasizing that the fundamental aim of the statute is to assist shareholders confronted with a tender offer in making "a decision whether to accept or reject the tender offer" or "the investment decision—whether to retain the security or sell it." See, *e.g.*, S. Rep. No. 550, 90th Cong., 1st Sess. 2-3 (1967); H.R. Rep. No. 1711, 90th Cong., 2d Sess. 2-3 (1968), *reprinted in* [1968] U.S. Code Cong. & Ad. News 2811, 2812-13.

which the target corporation shareholders *relied*.' " 619 F.2d at 195 (*quoting Chris-Craft Industries, Inc.* v. *Piper Aircraft Corp.*, 480 F.2d 341 (2d Cir.), *cert. denied*, 414 U.S. 910 (1973); footnote omitted). And the Second Circuit was further indisputably correct in its common-sense conclusion that: "In the instant case, the target's shareholders simply could not have relied upon McGraw-Hill's statements, whether true or false, since they were never given an opportunity to tender their shares"; "no reliance was possible under any imaginable set of facts." *Id.* Petitioners below, however, citing *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128 (1972), contended that they were excused from pleading reliance because that element is "presumed" once the omission of a "material" fact is shown. This argument was quite correctly rejected by both the District Court and the Court of Appeals in that the *Ute* presumption is not remotely applicable to the case at bar. For the express premise of *Ute* is that investors were forced to make investment decisions without disclosure of "material facts that reasonably could have been expected to influence their decisions to sell." *Id.* at 153. As this Court in *Ute* formulated the presumption:

> Under the circumstances of this case, involving primarily a failure to disclose, positive proof of reliance is not a prerequisite to recovery. All that is necessary is that the facts withheld be material in the sense that a *reasonable investor might have considered them important in the making of this decision* [to sell the UDC stock].
>
> *Id.* at 153-54 (emphasis supplied).*

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* Indeed, petitioners' bland assumption of "materiality" is itself highly questionable under the precedents. Thus, this Court's definition of materiality in the proxy context in *TSC Industries, Inc.* v. *Northway, Inc.*, 426 U.S. 438, 449 (1976) that an "omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote," presupposes the occurrence of a "vote." See also *Maldonado* v. *Flynn*, 597 F.2d 789, 795-96 (2d Cir. 1979) (false statement cannot be "material" under proxy laws unless shareholders are in fact being called upon to cast a vote). The test of "materiality" for

In other words, under the *Ute* rationale, where an investor was in fact engaged in "the making of [an investment] decision", he may under certain circumstances be "presumed" to have relied upon material nondisclosure. But manifestly that rationale has no applicability whatsoever in a case such as that at bar where neither petitioners nor any other McGraw-Hill shareholders were ever called upon to make an investment decision with respect to the proposed Amexco tender offer which never took place. As the Second Circuit accurately reasoned:

> These cases [of the Supreme Court], however, in presuming reliance, did not abolish it as an element of the cause of action. Rather, they held that in cases in which reliance is possible, and even likely, but is unduly burdensome to prove, the resulting doubt would be resolved in favor of the class the statute was designed to

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Section 14(e)'s tender offer provisions parallels that under Section 14(a)'s proxy provisions. See, *e.g.*, *Seaboard World Airlines, Inc.* v. *Tiger International, Inc.*, 600 F.2d 355, 360-61 (2d Cir. 1979). The Second Circuit there ruled that under Section 14(e) itself "a misstatement or omission is ' "material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding" ' whether to accept the tender offer", thereby recognizing that "materiality" can only exist when a shareholder is in fact being called upon to make an investment decision whether to tender. 600 F.2d at 361 (*quoting* the *TSC* definition of materiality as excerpted in *Prudent Real Estate Trust* v. *Johncamp Realty, Inc.*, 599 F.2d 1140, 1146 (2d Cir. 1979); footnote omitted).

Similarly, if the issue is phrased in terms of "causation", it could not be contended that it was the alleged "deception" that "caused" Amexco to abandon its proposal. As the District Court correctly set forth:

> [A]ny suggestion that AMEXCO withdrew its proposed tender offer in *reliance* upon the alleged McGraw-Hill representations and omissions would be absurd.
>
> (Emphasis in original.)

The District Court's conclusion that petitioners could not rationally establish legal causation is in full accord with the views of other courts that have had occasion to focus on the question in like circumstances. See, *e.g.*, *Rediker* v. *Geon Industries, Inc.*, 464 F. Supp. 73, 82 (S.D.N.Y. 1978); *Altman* v. *Knight*, 431 F. Supp. 309, 314 (S.D.N.Y. 1977); *Hundahl* v. *United Benefit Life Insurance Co.*, 465 F. Supp. 1349, 1369-70 (N.D. Tex. 1979).

> protect. [*Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375, 385 (1970).] We therefore presume reliance only "where it is logical" to do so. [*Chris-Craft Industries, Inc.* v. *Piper Aircraft Corp.*, 480 F.2d 341, 375 (2d Cir.), *cert. denied*, 414 U.S. 910 (1973).] Here, where no reliance was possible under any imaginable set of facts, such a presumption would be illogical in the extreme.
>
> 619 F.2d at 195.

3. "In connection with."

In seeking to ascertain the proper bounds of any "implied" damage remedy under Section 14(e), the starting point must be the plain language of Section 14(e) itself. *Piper* v. *Chris-Craft Industries, Inc.*, 430 U.S. 1, 24 (1977). Section 14(e) by its terms is limited to conduct

> *in connection with any tender offer* or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of *any such offer*, request, or invitation.
>
> 15 U.S.C. § 78n(e)
> (emphasis supplied).

This congressional language clearly presupposes the existence of an actual, effective "tender offer". Nothing in the statute's terms purports to extend its reach to *proposed* tender offers, like Amexco's, which in ultimate fact are *never made*. And the Second Circuit—in the after-the-fact damage context of the present action—quite correctly declined to read any such extension into the statute.* In this connection, it may be noted

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* The Second Circuit in its *per curiam* opinion did not explicitly hold that petitioners' complaint was subject to dismissal for failure to satisfy the "in connection with" requirement of Section 14(e). Nonetheless, such holding would appear to be a clear implication from the opinion. Thus: (1) the opinion distinguishes the case at bar from other hypothetical factual situations in which the Second Circuit states the "in connection with a tender offer" requirement *could* be met (619 F.2d at 195); and (2) the Second Circuit concludes its opinion with the statement "since American Express never made its proposed offer to the shareholders of McGraw-Hill, plaintiffs cannot state a cause of action for alleged misstatements under the Williams Act." *Id.* at 195-96.

again that in *Chris-Craft*, 430 U.S. at 35, this Court set forth that: "[T]he *sole* purpose of the Williams Act was the protection of investors *who are confronted with a tender offer*." (Emphasis supplied.) As noted,* this reading of Section 14(e) is in full accord with its legislative history. Thus, under the plain language of Section 14(e) as well as its legislative history and authoritative construction by this Court, no tender offer ever having taken place, defendants' supposed misconduct could not be "in connection with" a "tender offer".* *

4. This Court's *Blue Chip* decision.

Section 14(e)'s "in connection with any tender offer" clause has a well-known predecessor and close cognate in Rule 10b-5's clause requiring that the conduct proscribed by that Rule be "in connection with the purchase or sale of any security."* * * It is now quite settled that Rule 10b-5's "in connection with" requirement is to be strictly enforced in damage actions brought under that Rule: the plaintiff in such

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* See 12n.* *supra*.

* * It should be noted that in a footnote in a subsequent *amicus* brief in the Seventh Circuit, Brief of the Securities and Exchange Commission, 20 n.25, *Weiss* v. *Marshall Field & Co.*, Nos. 80-1375, 80-1389 (7th Cir., appeals docketed March 21 and 24, 1980), the Securities and Exchange Commission has expressed the view that the Second Circuit's opinion in the present case should be narrowly read to rest upon issues of absence of "reliance" and "causation" only. With respect to the "in connection with" issue, the SEC's *amicus* brief states:

> In any event, if the *Lewis* decision is read as holding that Section 14(e) does not extend to deception in connection with tender offer proposals where shareholders are not given an opportunity to tender to the bidder, the Commission submits that the decision is in error.
>
> *Id.* at 21 n.25.

* * * Except for the different wording of their "in connection with" clauses, Section 14(e) and Rule 10b-5 are, of course, substantially identical. Compare 15 U.S.C. § 78n(e) with 17 C.F.R. § 240.10b-5. See *Seaboard World Airlines, Inc.* v. *Tiger International, Inc.*, 600 F.2d 355, 358 n.3 (2d Cir. 1979); *Electronic Specialty Co.* v. *International Controls Corp.*, 409 F.2d 937, 940-41 (2d Cir. 1969).

an action must show that he is a purchaser or seller of a security; it simply will not suffice for a Rule 10b-5 plaintiff to show that a defendant caused him *not* to purchase, or *not* to sell, a security. That is, of course, the teaching of this Court's decision in *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723 (1975), where it was held that fraudulent misrepresentations which succeeded in preventing a "purchase" of a security from ever taking place did not thereby give rise to any violation of Rule 10b-5. *Id.* at 752-55. See also, *e.g.*, *Iroquois Industries, Inc.* v. *Syracuse China Corp.*, 417 F.2d 963, 966-69 (2d Cir. 1969), *cert. denied*, 399 U.S. 909 (1970); *Greenstein* v. *Paul*, 400 F.2d 580, 581 (2d Cir. 1968); *Mutual Shares Corp.* v. *Genesco, Inc.*, 384 F.2d 540, 544 & n.14 (2d Cir. 1967); *Birnbaum* v. *Newport Steel Corp.*, 193 F.2d 461, 462-63 (2d Cir.), *cert. denied*, 343 U.S. 956 (1952). Thus, existing Rule 10b-5 "in connection with" doctrine, if analogically applied here, independently compelled dismissal of petitioners' Section 14(e) claim: if "fraud" which prevents a purchase of securities from taking place is not "in connection with" the purchase of a security, then "fraud" which prevents a tender offer from taking place is not "in connection with" a tender offer.

5. The *Applied Digital* decision.

In their certiorari petition, petitioners appear to contend that the Second Circuit's decision is in conflict with a decision of Judge Weinfeld of the Southern District of New York in *Applied Digital Data Systems Inc.* v. *Milgo Electronic Corp.*, 425 F. Supp. 1145 (S.D.N.Y. 1977), allowing Section 14(e) to be invoked, upon an *injunction* motion, where a proposed tender offer, albeit imminent, had not yet taken place. See Petition, pp. 7-8. There is no conflict: indeed, the opinion of the Second Circuit expressly notes that Court's *agreement* with Judge Weinfeld's view in *Applied Digital*. 619 F.2d at 195. The *Applied Digital* case is simply inapposite to the present petitioners' after-the-fact action for *damages*. The injunction-

damages distinction, repeatedly enunciated by the courts in this area of the law, is here determinative.*

In *Applied Digital*, Judge Weinfeld granted the motion of a prospective tender offeror for a Section 14(e) preliminary injunction to restrain a target corporation from issuing a substantial block of stock to a friendly party in an alleged bad-faith effort to thwart the proposed tender offer. While the tender offer had not yet technically commenced, the movant demonstrated to Judge Weinfeld's satisfaction: (1) that the commencement of the tender offer in fact was "imminent"; (2) that substantial evidence supported the movant's contention that the target company's plan to issue the stock in question actually was a bad-faith maneuver designed to interfere with the proposed tender offer; and (3) that the "balance of hardships" tipped decidedly in the movant's favor. *Id.* at 1154, 1158-59, 1161-62.

The *Applied Digital* decision is undoubtedly correct: a request for a preliminary injunction necessarily addresses the *future*. Accordingly, a judge faced with a "good faith" proposal to make an "imminent" tender offer, *id.* at 1154, can only assume (absent any contrary indications, of which there were none in *Applied Digital*) that the proposed tender offer in due course will become an actual tender offer. Further, it is obvious that pre-tender offer conduct directed at a proposed offer may, when the offer attains actuality, affect the investment decision which then will confront the

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* In *Chris-Craft*, this Court expressly recognized the importance of the injunction-damages distinction in this area. Although refusing to imply an after-the-fact damage action under Section 14(e) in favor of a defeated tender offeror, this Court approvingly cited the Circuit's decision in *Electronic Specialty Co.* v. *International Controls Corp.*, 409 F.2d 937, 947 (2d Cir. 1969), which permitted a target corporation and a non-tendering shareholder-offeree to seek an injunction under Section 14(e) and expressly quoted Judge Friendly's observation there that "in corporate control contests the stage of preliminary injunctive relief, *rather than post-contest lawsuits*, 'is the time when relief can best be given.' " 430 U.S. at 42 (emphasis supplied). Thus, the distinction between injunctive and compensatory relief is critical to the scope of Section 14(e).

shareholder-offerees—the very investment decision the integrity of which the Williams Act is concerned to protect. As Judge Weinfeld observed in *Applied Digital*:

> Although the shareholders might not in the pre-offer period be faced with a present decision whether to exchange their stock in the target corporation, statements and actions of the target corporation and the offeror during this period *clearly have the capacity to affect any future decision and should thus fall within the purview of the statute.*
>
> 425 F. Supp. at 1154 (emphasis supplied).

The principles which underlie *Applied Digital*, however, have nothing to do with the case that was before the Second Circuit. This case invokes the *past*, not the future: the Amexco/McGraw-Hill affair is history and we are privileged to *know* that no tender offer ever occurred. And, precisely because no tender offer occurred, the investment decision which is the focus of the Williams Act and which concerned Judge Weinfeld in *Applied Digital* never confronted petitioners or any other McGraw-Hill shareholders.

Judge Weinfeld's reasoning with respect to the "in connection with" requirement of Section 14(e) is instructive:

> There is no apparent reason why any given action may not be taken "in connection with" a development reasonably certain to take place in the future. . . . Indeed, Rule 10b-5, . . . after which section 14(e) was closely patterned, requires that a complained of action take place "in connection with the purchase or sale of a security," yet it repeatedly has been held to create a cause of action *to enjoin* purchases or sales of securities that have been *proposed but not yet effected.*
>
> 425 F. Supp. at 1153 (emphasis supplied; footnotes omitted).

And the line of cases relied upon in *Applied Digital* makes clear that it is *only* where judicial intervention is sought in order *to prevent a threatened future fraud* that the "in connection with" requirement of Rule 10b-5 may properly be "relaxed" (*i.e.*, a plaintiff need not complain of an actual purchase or sale of securities). See *Mutual Shares Corp.* v. *Genesco, Inc.*, 384 F.2d 540, 546-47 & n.25 (2d Cir. 1967); *Ruckle* v. *Roto American Corp.*, 339 F.2d 24 (2d Cir. 1964). Accord, *e.g.*, *Tully* v. *Mott Supermarkets, Inc.*, 540 F.2d 187, 194-95 (3d Cir. 1976); *Kahan* v. *Rosenstiel*, 424 F.2d 161, 173 (3d Cir.), *cert. denied*, 398 U.S. 950 (1970); *Iroquois Industries, Inc.* v. *Syracuse China Corp.*, 417 F.2d 963, 968 (2d Cir. 1969), *cert. denied*, 399 U.S. 909 (1970); *Fuchs* v. *Swanton Corp.*, 482 F. Supp. 83, 89-90 (S.D.N.Y. 1979); *Berne Street Enterprises, Inc.* v. *American Export Isbrandtsen Co.*, [1969-1970 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 92,711, at 99,134 (S.D.N.Y. 1970) (Mansfield, J.). No such relaxation is permissible in an after-the-fact suit for damages where it is conceded that no tender offer ever took place.

POINT II

Petitioners' complaint was required to be dismissed under the principles of *Santa Fe Industries, Inc.* v. *Green.*

In *Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462 (1977), this Court held that Section 10(b) of the Securities Exchange Act does not reach cases "in which the essence of the complaint is that shareholders were treated unfairly by a fiduciary", *id.* at 477, and that a Rule 10b-5 claim is stated "only if the conduct alleged can be fairly viewed as 'manipulative or deceptive' within the meaning of the statute." *Id.* at 473-74. It would appear clear that the principles of *Santa Fe* are fully applicable to actions brought under Section 14(e). See, *e.g.*, *Bucher* v. *Shumway*, [1979-80 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 97,142, at 96,299 (S.D.N.Y. 1979), *aff'd on the opinion below*, 622 F.2d 572 (2d Cir.), *cert. denied*, 49 U.S.L.W. 3247 (Oct. 6, 1980); *In re Sunshine Mining Co. Securities Litigation*, [1979-80 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 97,217, at 96,635-36 (S.D.N.Y. 1979); *Marshel* v. *AFW Fabric Corp.*, 441 F. Supp. 299, 300 (S.D.N.Y. 1977).

Since *Santa Fe*, the lower courts have repeatedly been faced with actions which have sought to circumvent this Court's holding and foist jurisdiction upon the federal courts by insertion of allegations of "deception" or "omission" in complaints which fundamentally have as their gravamen claims of breach of fiduciary duty by defendants. Generally, such attempts have been rejected by the lower courts which have ruled that, whatever other allegations are pleaded, whenever the "essence" or "central thrust" of a purported federal securities law complaint is fiduciary breach, or where the complaint "amounts to no more than" or "boils down to" such a claim, *Santa Fe* requires dismissal. See, *e.g.*, *Biesenbach* v. *Guenther*, 588 F.2d 400, 402 (3d Cir. 1978); *Hundahl* v. *United Benefit Life Insurance Co.*, 465 F. Supp. 1349, 1362 (N.D. Tex. 1979); *Bucher* v. *Shumway*, [1979-80 Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 97,142, at 96,299-303 (S.D.N.Y. 1979), *aff'd on the opinion below*, 622 F.2d 572 (2d Cir.), *cert. denied*, 49 U.S.L.W. 3247 (Oct. 6, 1980); *In re Sunshine Mining Co. Securities Litigation*, [1979-80

Transfer Binder] CCH Fed. Sec. L. Rep. ¶ 97,217, at 96,635-36 (S.D.N.Y. 1979); *Altman* v. *Knight*, 431 F. Supp. 309, 311, 313-14 (S.D.N.Y. 1977).

The issue, however, has not been free of difficulty and certain cases have tended to give a very narrow reading to this Court's *Santa Fe* holding. See, *e.g.*, dissenting opinion of Meskill, C.J., in *Goldberg* v. *Meridor*, 567 F.2d 209, 225 (2d Cir. 1977), *cert. denied*, 434 U.S. 1069 (1978); *Jones* v. *National Distillers & Chemical Corp.*, 484 F. Supp. 679, 685 (S.D.N.Y. 1979); *cf. Hundahl* v. *United Benefit Life Insurance Co.*, 465 F. Supp. 1349, 1365 (N.D. Tex. 1979).

In the case at bar, respondents contended in the District Court that petitioners' complaint in substance presented a garden-variety claim for breach of fiduciary duty by directors and that petitioners' allegations of "deception" were of a "bootstrap" nature amounting upon close analysis to nothing more than claims that respondents had failed to "disclose" that their rejection of the Amexco proposals was the product of a breach of fiduciary duty. Judge Motley in the District Court, however, citing to one of her own prior precedents and believing cases relied upon by respondents to be distinguishable, rejected this challenge to the complaint and ruled that the complaint alleged "misstatements and omissions actionable under Section 14(e)." ¶ 97,195 at 96,569. The District Court, of course, nonetheless dismissed the complaint on alternative grounds.

Petitioners in the Second Circuit renewed their challenge to the complaint on *Santa Fe* grounds. The Second Circuit, in upholding dismissal of the complaint for failure to satisfy the Section 14(e) requirements of "reliance" and "in connection with", did not comment upon the *Santa Fe* issue.

Were this Court to accept this case for review, respondents (in supporting the judgment under review) would ask this Court to make clear that its holding in *Santa Fe* cannot be subverted by mere "bootstrap" allegations of "deception" and to rule that petitioners' complaint was subject to dismissal on this ground as well.

POINT III

There is a serious question whether Section 14(e) provides a shareholder of a target company with any implied cause of action for damages.

In *Piper* v. *Chris-Craft Industries, Inc.*, 430 U.S. 1 (1977), this Court specifically held that a competing tender offeror has no implied damage action under Section 14(e). The opinion expressly left undecided whether either "shareholder-offerees" or target corporations have such an implied action. 430 U.S. at 38-39 & n.25, 42 n.28. Cf. *Stull* v. *Bayard*, 561 F.2d 429, 432 (2d Cir. 1977), *cert. denied*, 434 U.S. 1035 (1978) (assumed but did not decide that target shareholders had a right to sue under Section 14(e)). Subsequent decisions of this Court, however, strongly suggest that no damage action of any kind is necessarily implicit in Section 14(e).

In *Touche Ross & Co.* v. *Redington*, 442 U.S. 560 (1979), reversing a Second Circuit finding of an implied cause of action for damages under Section 17(a) of the Securities Exchange Act, this Court acknowledged that it had abandoned the permissive analysis for implication of private causes of action that it had employed in *J.I. Case Co.* v. *Borak*, 377 U.S. 426 (1964) to imply a cause of action under Section 14(a). 442 U.S. at 578; see also *Cannon* v. *University of Chicago*, 441 U.S. 677, 735-36 & n.6 (1979) (Powell, J., dissenting, describes *Borak* as "unprecedented and incomprehensible" [footnote omitted]). This Court in *Redington* further explained that in recognizing an implicit damage action under Section 10(b), it "simply explicitly acquiesced in the 25-year-old acceptance by the lower federal courts of an implied action under" that section. *Id.* at 577 n.19. No such "history of longstanding lower court interpretation", *id.*, exists with respect to Section 14(e), which was not enacted until 1968.

The Court reaffirmed and perhaps stiffened its resistance to implied damage actions under the securities laws in *Transamerica Mortgage Advisors, Inc. (TAMA)* v. *Lewis*, 444 U.S. 11 (1979). *TAMA* refused to imply a cause of action

for damages under Section 206 of the Investment Advisers Act of 1940 (an antifraud statute closely resembling Section 14(e) and Rule 10b-5) notwithstanding that the plaintiff concededly belonged to the class protected by the statute. *Id.* at 18-19.

It would thus appear that there is a serious question whether Section 14(e) should be read to imply any damage action in favor of a target company shareholder. Respondents did not advance this argument to the District Court in support of dismissal. The *Redington* and *TAMA* cases were decided by this Court prior to briefing of the appeal in the Second Circuit. In their brief to the Second Circuit, respondents "noted in passing that, in light of recent specific Supreme Court holdings in securities laws cases and the trend of securities law cases in that Court, it is by no means clear that *any* state of facts will give rise to an 'implied' damage remedy under Section 14(e)." The Second Circuit, in affirming the dismissal of the complaint upon alternative grounds, did not directly comment upon the issue but in dictum indicated that in certain circumstances it believed an implied action for damages under Section 14(e) could lie in favor of an aggrieved shareholder.

Were this Court to accept this case for review, respondents would ask this Court to clarify whether Section 14(e) is to be read to give rise to any implied cause of action for damages.

SUMMARY

Respondents submit that this case was correctly decided by the Second Circuit. Should this Court determine to grant certiorari, respondents submit that the ultimate result would be affirmance of the dismissal of petitioners' complaint. Respondents choose to take no position as to whether this Court should grant certiorari in order to express its views on the various questions of statutory interpretation presented by this action.

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Respectfully submitted,

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